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No. 83-1561

IN THE

Supreme Court of the United States

OCTOBER TERM, 1983

COMMISSIONER OF INTERNAL REVENUE,

Petitioner,

v.

ESTATE OF ADA E. VAN HORNE, DECEASED, ROBERT L. FARMER AND RICHARD R. COLE, EXECUTORS,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF IN OPPOSITION

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April 18, 1984

QUESTION PRESENTED

Under the provisions of Section 2053(a)(3) of the Internal Revenue Code of 1954, a federal estate tax deduction is allowed "for claims against the estate". The question presented is whether that section requires that an allowable and enforceable claim for a lifetime annuity be valued as of the date of death solely by use of actuarial tables, or whether events occurring after the decedent's death may be considered in establishing a different value for that claim.

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BRIEF IN OPPOSITION

STATEMENT OF THE CASE

The facts material to consideration of the question presented have been fully and accurately set forth in the Statement of the Commissioner of Internal Revenue ("the Commissioner") contained in the petition (petition at 2, 3). The Statement also fairly summarizes the holdings of the

Tax Court and the Ninth Circuit on the question presented (petition at 3, 4, 5). Both lower courts determined that the principles established by this Court in *Ithaca Trust Co. v. United States*, 279 U.S. 151 (1929) were controlling and dispositive of the case at bar (App. at 3a, 5a, 6a; at 19a, 22a).[1]

REASONS FOR DENYING THE WRIT

I. FOR FEDERAL ESTATE TAX PURPOSES, THE LAW IS SETTLED THAT A VALID AND ENFORCEABLE CLAIM FOR A LIFETIME ANNUITY MUST BE VALUED AS OF THE DATE OF DEATH BY USE OF ACTUARIAL TABLES.

A. In 1929, this Court decided *Ithaca Trust Co. v. United States*, 279 U.S. 151 (1929). There, the testator gave his wife a life estate in the residue of his estate, together with a limited right to invade principal for her benefit. On her death, the estate remainder was to pass to charitable beneficiaries.[2] The wife, in fact, died within six months of the testator's death and prior to the due date of the estate's federal estate tax return.

In order to compute the federal estate tax charitable deduction, there was apparent agreement that the wife's life estate must first be valued. The life estate would then be subtracted from the residue of the estate to determine the value of the deductible charitable remainder.

The issue presented to this Court was the proper manner of valuing the wife's life estate. The testator's estate claimed an enlarged charitable deduction based upon the wife's death before the expiration of her life expectancy. The government

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[1] Citations to "App" are to the appendix to the petition and are the same in form as those in the petition. Unless otherwise noted, all statutory references are to the Internal Revenue Code of 1954 (26 U.S.C.), as amended (the Code or I.R.C.).

[2] The Court held that the limited right to invade principal for the benefit of the wife did not make the charitable gifts so uncertain as to preclude any estate tax charitable deduction therefor. *Ithaca Trust Co. v. United States*, 279 U.S. 151, 154 (1929).

sought to limit the charitable deduction by claiming that the life estate had to be valued as of the testator's date of death without reference to facts known when the estate tax return was filed.

This Court, in holding that the wife's life estate had to be valued as of the testator's death by use of actuarial tables, stated:

> "The second question is raised by the accident of the widow having died within the year granted by the statute sec. 404, and regulations, for filing the return showing the deductions allowed by sec. 403, the value of the net estate and the tax paid or payable thereon. By sec. 403(a)(3) the net estate taxed is ascertained by deducting among other things gifts to charity such as were made in this case. But as those gifts were subject to the life estate of the widow of course their value was diminished by the postponement that would last while the widow lived. The question is whether the amount of the diminution, that is, the length of the postponement, is to be determined by the event as it turned out, of the widow's death within six months, or by mortality tables showing the probabilities as they stood on the day when the testator died. The first impression is that it is absurd to resort to statistical probabilities when you know the fact. But this is due to inaccurate thinking. The estate so far as may be is settled as of the date of the testator's death. *** The tax is on the act of the testator not on the receipt of property by the legatees. *** Therefore the value of the thing to be taxed must be estimated as of the time when the act is done. But the value of property at a given time depends upon the relative intensity of the social desire for it at that time, expressed in the money that it would bring in the market. *** Like all values, as the word is used by the law, it depends largely on more or less certain prophecies of the future, and the value is no less real at that time if later the prophecy turns out false than when it comes out true. *** Tempting as it is to correct uncertain probabilities by the now certain fact, we

are of opinion that it cannot be done, but that the value of the wife's life interest must be estimated by the mortality tables. Our opinion is not changed by the necessary exceptions to the general rule specifically made by the Act." 279 U.S. at 154-155.

In addition to determining the valuation issue presented for decision, *Ithaca Trust* enunciated the following principles which remain an integral part of the system of federal estate tax administration:

(i) The estate so far as may be is settled as of the date of the testator's death; and

(ii) Where death of the measuring life is the only factor affecting valuation, actuarial tables must be used to determine a sum certain date of death value.

These principles will be discussed throughout the remainder of this brief.

The applicability of *Ithaca Trust* to the valuations of "claims against the estate" has been considered in a number of lower court proceedings [e.g., *Propstra v. United States*, 680 F. 2d 1248 (9th Cir. 1982); *Commissioner v. Estate of Shively*, 276 F. 2d 372 (2d Cir. 1960)]. In only one case, *Estate of Lester v. Commissioner*, 57 T.C. 503 (1972), however, was any federal court presented with the issue of valuing a claim for a lifetime annuity where there was no variable other than the death of the annuitant.

The claim to be valued in *Estate of Lester*, like the claim in the case at bar, was an obligation to make periodic payments under a divorce decree. The decree provided for the payment of $1,000 per month to the former wife until the earlier of her death or the expiration of 130 months. If the husband died before completion of the required payments, his estate was to discharge the obligation. The husband died after making only 19 monthly payments. Thereafter, the decedent's estate made ten payments, then purchased a commercial annuity to cover the balance of the obligation. The executor claimed an

estate tax deduction of $111,000 ($1,000 x 111 months remaining at the husband's death) for the obligation under the divorce decree. During audit review of the estate tax return, the executor contended, as an alternative theory in support of an enlarged deduction, that the estate should be allowed a deduction equal to the sum of the monthly payments made by the estate and the purchase price of the annuity. The Commissioner, contrary to his position herein, urged that *Ithaca Trust* required that the claim be valued as of the date of death by use of actuarial tables. The Tax Court, in sustaining the Commissioner's contention, stated:

> "The *Ithaca Trust Co.* case indeed establishes the general principle that we must apply, if, as in the case before us, on the date of death the estate's obligation is one which will be satisfied in the future. The use of actuarial tables such as those found in section 20.2031-7, Estate Tax Regs., to ascertain the value of such a claim, especially when it is periodic in nature, has been the administrative and judicial norm for many years.***
>
> "We think there is no reason in this case to go beyond the principle of *Ithaca Trust Co. v. United States, supra* — that the value of the judgment in the divorce proceedings is to be determined as of the date of the husband's death by the use of the tables employed here by the Commissioner, which take into consideration the contingency of the wife's death prior to final payment of the installments to become due.
>
> "There is no need to go into the effect of events subsequent to the husband's death, i.e., how the estate finally freed itself of a continuing and admitted liability.
>
> "Here the validity of the claim is undisputed. The estate acknowledged it in the estate tax return and subsequently made payments thereon. The only question is how the claim should be valued for the purpose of determining the amount of the estate tax deduction. Under *Ithaca Trust Co.* this is to be done as of the time of death. Petitioner cites us

to no case or other authority which would show error in the Commissioner's determination and we have found none." 57 T.C. at 507.

The government, in the administration of the federal tax laws, has followed the *Ithaca Trust* principle recognizing the validity of valuations made by use of actuarial tables. The regulations promulgated under Section 2031 include the actuarial tables to be employed for estate and gift tax purposes. Moreover, in Rev. Rul. 80-80, 1980-1 Cum. Bull. 194, the government reaffirmed its long-held position that actuarial tables "are to be used in valuing annuities, life estates, terms for years, remainders, and reversions", stating at page 194:

> "The actuarial tables in the regulations are provided as an administrative necessity, and their general use has been readily approved by the courts. See *Ithaca Trust Company v. United States*, 279 U.S. 151 (1929); ***"

The ruling, after reviewing a series of cases considering when departure from use of the tables was proper, enunciated the following principle at page 195:

> "In view of recent case law, the resulting principle is as follows: the current actuarial tables in the regulations shall be applied if valuation of an individual's life interest is required for purposes of the federal estate or gift taxes unless the individual is known to have been afflicted, at the time of transfer, with an incurable physical condition that is in such an advanced stage that death is clearly imminent. Death is not clearly imminent if there is a reasonable possibility of survival for more than a very brief period. ***
>
> "The above principle is applicable to every situation that involves valuation of an interest that is dependent upon the life of one or more individuals for federal estate or gift tax purposes, including valuation with respect to deductions allowable under section 2055 or section 2522 of the Code, with the exception of determinations involving a

decedent's own life expectancy under sections 2037 and 2042(2)."

In the case at bar, it is clear that, at Ada's death, James's death was not so imminent as to bring the case within the exception set forth in Rev. Rul. 80-80. (App. at 10a, 11a). In none of the proceedings below did the Commissioner so contend. The ruling's general principle is that, with the exception of certain sections not pertinent herein, the actuarial tables must be used in "every situation that involves valuation [of an annuity] for federal estate and gift tax purposes, including [but not limited to] valuation with respect to deductions allowable under section 2055 or section 2522 of the Code". Therefore, by the government's own ruling, the valuation of James's claim for a lifetime annuity must be made, for purposes of Section 2053, by use of its actuarial tables.

B. The Commissioner, in attempting to avoid the clear mandate of *Ithaca Trust*, contends that the Court of Appeals decision below conflicts with those of a number of other circuits. An analysis of the cases relied upon by him (petition at 5-13), however, discloses (i) that all of them are factually distinguishable from the case at bar, and (ii) that none dealt with the issue of valuation presented herein.

Section 2053(a)(3) provides an estate tax deduction for such amounts of "claims against the estate • • • as are allowable by the laws of the jurisdiction • • • under which the estate is being administered." The regulations promulgated thereunder specify that claims, to be deductible, must "represent personal obligations of the decedent existing at the time of his death." Moreover, "[o]nly claims enforceable against the decedent's estate may be deducted." Treas. Reg.§ 20.2053-4.

Section 2053 also allows a deduction for funeral expenses and administration expenses. As in the case of claims which are unmatured, contingent, or disputed at the date of death, those expenses are inherently dependent upon post-death facts to determine whether, and to what extent, they are "allowable".

The threshold issue, then, in determining the deductibility of a claim is its "allowability" or "enforceability" against the decedent's estate. The facts in this case clearly demonstrate that James's claim met those tests (App. at 2a, 10a), and the Tax Court below noted that this case presented the single issue of the proper valuation of an allowable and enforceable claim for a lifetime annuity (App. at 14a).

The Commissioner, from the voluminous precedents cited in the proceedings below, gleaned five Court of Appeals decisions which he urges are in conflict with the Court of Appeals decision herein. Two other decisions, including a Ninth Circuit decision cited in this case, were discussed in the petition (petition at 5-9). None of those cases, however, involved an enforceable claim where, as here, the only post-death factor to be evaluated is the death of a measuring life.[3]

The seven Court of Appeals decisions discussed at pages 5 through 9 of the petition, none of which involved a claim which was contingent, unmatured, or disputed at the date of death, arrange themselves into two distinct categories. The first encompasses claims valid and enforceable at the date of death which were subsequently reduced or eliminated by the voluntary action of the affected party. The second category contains enforceable claims which were compromised after death. There is disagreement among the circuits within each category as to whether post-death facts are to be considered in determining the amount deductible under Section 2053 (and its predecessor sections) of the Code.

The following Court of Appeals decisions held that post-death facts are to be considered in valuing a deductible claim where, following death, the claimant's voluntary actions affect the estate's obligation to the claimant: *Commissioner v. Estate of Shively*, 276 F. 2d 372 (2d Cir. 1960) (alimony claim

[3] Unlike the factual patterns developed in the Court of Appeals decisions relied upon by the Commissioner, James's claim herein was valid and enforceable at Ada's death *and* was fully enforced and paid in accordance with its precise terms.

was payable for life or until remarriage; widow chose to and did remarry prior to estate tax return due date; deduction was held to be limited to amounts actually paid); *Estate of Hagmann v. Commissioner*, 60 T.C. 465 (1973), aff'd per curiam, 492 F. 2d 796 (5th Cir. 1974) (no deduction was allowed where, following death, no claims for valid debts were filed against the estate and no amounts were paid by the estate); and *Jacobs v. Commissioner*, 34 F. 2d 233 (8th Cir. 1929), cert. denied, 280 U.S. 603 (1929) (no deduction was allowed where, following death, claimant abandoned contractual claim in favor of rights under decedent's Will). In *Commissioner v. Strauss*, 77 F. 2d 401 (7th Cir. 1935), opinion withdrawn, 81 F. 2d 1016 (7th Cir. 1936), the Court of Appeals for the Seventh Circuit sustained a full deduction for a claim on facts substantially similar to those in *Estate of Hagmann v. Commissioner, supra.*

In the second category, which involves post-death compromises of claims, the following Court of Appeals decisions held that post-death facts are to be considered in valuing claims: *Commissioner v. State Street Trust Co.*, 128 F. 2d 618 (1st Cir. 1942) (alimony claim under court decree was for life, subject to modification upon remarriage; estate, following compromise of alimony claim, was allowed a deduction measured on the amount provided in the compromise agreement); *Estate of Metcalf v. Commissioner*, 7 T.C. 153 (1946), aff'd by order, 47-2 U.S. Tax Cas. (CCH) ¶ 10,566 (6th Cir. 1947) (liens against decedent's real property were compromised for reduced amounts; estate's deduction was limited to amounts paid). The Ninth Circuit, in a decision cited in its own opinion below, determined that a decedent's estate was entitled to a deduction for the full date of death value of a certain and enforceable lien claim against estate real property, notwithstanding the fact that the claim was subsequently settled by the estate for a reduced amount. *Propstra v. United States*, 680 F. 2d 1248 (9th Cir. 1982).

As demonstrated above, not one single Court of Appeals case has considered the issue herein presented — the valuation of a life annuity claim where the only post-death factor is the death of the claimant. Therefore, there can be no conflict between the decision of the Ninth Circuit below and those of other circuits which, for its resolution, requires that this Court grant the Commissioner's petition for writ of certiorari.

C. In a final and futile attempt to avoid the *Ithaca Trust* precedent, the Commissioner has contended that the Court's decision has limited applicability — that it applies to cases involving valuation of charitable, but not other, deductions (petition at 13). The same argument was made unsuccessfully to the Tax Court below, which declared with great perception:

> "It is one thing to distinguish *Ithaca Trust* in cases involving enforceability of a claimed debt, but to distinguish it here would be to distinguish it to the point of extinction." (App. at 22a).[4]

II. THE UNIQUE FACTS OF THIS CASE DO NOT PRESENT AN IMPORTANT QUESTION REQUIRING FURTHER ILLUMINATION BY THIS COURT.

As observed in Part I, during the 57-year period since *Ithaca Trust* was decided, only one reported federal case, *Estate of Lester v. Commissioner*, 57 T.C. 503 (1972), involving the valuation of an enforceable claim against an estate, presented a factual pattern substantially similar to the one here under review. The unique facts in this case are (i) an

[4] The position urged by the Commissioner here is at odds with the one he took in *Estate of Lester* where he argued *for* the applicability of actuarial tables in valuing claims against the estate. Perhaps the rule for which the Commissioner is advocating is better expressed as follows: The use of actuarial tables in valuing claims against the estate is proper if it is favorable to the government; valuation by actuarial tables is not proper if the tables do not favor the government.

enforceable alimony claim for a lifetime annuity which will terminate *only* upon the claimant's death (and not upon any other occurrence), and (ii) the termination of the estate's obligation to pay the lifetime annuity by the death of the claimant prior to the estate tax return date.

The Commissioner, contending that the question presented has administrative significance, claims that 43 cases similar to the case at bar involving more than $6 million in tax revenues are currently pending (petition at 15). The facts of those cases are not disclosed, so it is impossible to comment on them with particularity. In view of the dearth of past precedents involving the facts herein presented, however, it is very likely that those cases involve other issues (allowability or enforceability of a claim; valuation of an enforceable claim where factors other than the death of the claimant must be evaluated) which have been the subject of extensive litigation since the decision in *Ithaca Trust* was rendered.

The question herein presented is a pure valuation issue, and reported cases involving that issue alone are very rare. When a claim is for a sum certain, the amount of the claim itself resolves the valuation issue. When a claim is for a lifetime annuity, actuarial tables provide the recognized method for determining the claim's sum certain value. *Ithaca Trust*, in which this Court validated the use of actuarial tables to value lifetime rights to periodic payments, remains a viable and sufficient precedent. This case falls squarely within the *Ithaca Trust* rationale, and the question presented neither requires nor warrants further illumination by this Court of the principles it enunciated more than a half century ago.

III. RATIONAL AND EVEN-HANDED TAX ADMINISTRATION WOULD BE SIGNIFICANTLY IMPAIRED IF THE *ITHACA TRUST* RULE WERE LIMITED OR ALTERED AS ARGUED BY THE COMMISSIONER.

In the system of estate tax administration, actuarial tables have long provided the recognized method for valuing

annuities, life estates, terms of years, remainders, and reversions. *Ithaca Trust Co. v. United States,* 279 U.S. 151 (1929), confirmed the appropriateness of the actuarial valuation method which provides needed certainty and facilitates settlement of estates as of the decedent's death. The government's regulations under Section 2031 of the Code contains the tables applicable in the estate tax context, and Rev. Rul. 80-80, 80-1 Cum. Bull. 194, underscores the government's position that the tables are applicable in a wide variety of contexts, including the valuation of claims. (Also, see *Estate of Lester v. Commissioner, supra.*)

Application of actuarial tables, being based upon statistical averages, sometimes favors the government (e.g., *Ithaca Trust; Estate of Lester*), and in other instances their use favors the taxpayer (e.g., *Chauncey Stillman v. Commissioner,* T.C. Memo 1965-94, 24 TCM 478 (1965), where a gift tax deficiency in excess of $900,000 turned on whether the donated contingent remainder was to be valued actuarially or by recognition of the fact that the life tenant died within two months after the making of the gift and before the gift tax return was filed). The actuarial tables encompass the lives of all individuals, including those who die shortly after the valuation date and those who far outlive their life expectancies. It is their statistical breadth and uniform application, regardless of "windfall" or "detriment" in a particular case, which validate the use of those tables. This very point was emphasized in *Estate of Chauncey Stillman, supra,* where the Tax Court stated:

> "The use of mortality and actuarial tables in valuing a future interest dependent upon a life estate involves the use of established computations which seldom accurately predict the future in a particular situation or accurately determine value in a particular case, but the use of such established computations proves to be substantially correct when used in a great number of instances under the law of

averages; and the respondent's [the Commissioner's] position is that he deals with a great enough number of different taxpayers to eventually receive the benefit of the process of averages." 24 TCM at 503.[5]

In seeking a review of the Ninth Circuit decision below, the Commissioner is asking that this Court overturn or alter the principles it enunciated in *Ithaca Trust* — principles which have been the logical underpinnings of a rational system of tax administration for more than fifty years. If the Commissioner's position were sustained, current actuarial tables, based on all lives in being at death, would require revision to exclude from lives upon which they are based those persons who die within some "hindsight period". The length of the period will have to be defined — whether it expires on (i) the due date of the estate tax return, (ii) the date on which the tax liability is finally determined, (iii) the date on which the statute of limitations for estate tax deficiency assessments runs, or (iv) some other date. Whatever date is selected would impair the ability to settle estates "as of the date of the testator's death".

If the Commissioner is not seeking a revision of his own actuarial tables, he must instead be urging this Court to fashion an exception to its own reasoning in *Ithaca Trust* — that, at least in the valuation of claims, departure from the tables is proper where it produces a result favorable to the government. Such an exception would create a double standard — one set of rules for taxpayers, another for the government. Fairness, tax equity, and even-handed tax administration are cornerstones of public confidence in our system of taxation, and the exception urged by the Commissioner — which is unfair and illogical — would seriously and unnecessarily undermine that confidence. (See *Estate of*

[5] Individual taxpayers have less opportunity to derive the benefit of the process of averages than does the Commissioner — less opportunity to recoup if application of actuarial tables in a particular instance produces a favorable result for the government.

Lester v. Commissioner, 57 T.C. 503 (1972), where the Commissioner was the beneficiary of the valuation of a claim by use of actuarial tables.)

The cause of orderly tax administration has been admirably served by the principles established in *Ithaca Trust.* — (i) that a decedent's estate should be settled as of a decedent's date of death, and (ii) where death of the measuring life is the sole factor affecting valuation, actuarial tables must be used. The Commissioner has demonstrated no logical or compelling reason for overturning those principles to reach the result which he urges herein.

IV. CONCLUSION.

For the reasons stated, the Court should deny the Commissioner's petition for writ of certiorari.

Respectfully submitted,

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